

Overview of Minister Taxation

The presentation will begin shortly...



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CPE needed?

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Remote Accounting Services

- We provide bookkeeping services to churches and Christian nonprofits including:
 - Produce a monthly financial report for leadership
 - Process contributions and bills
 - Record all transactions in the general ledger
 - Reconcile bank accounts, credit cards, and close the books each month
 - Process payroll and file all quarterly and annual payroll forms
 - Provide budget and cash flow projection oversight
 - Give assistance with internal controls



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Remote Accounting Services

- Why do we provide this service?
 - With online software solutions dramatically improving, outsourced bookkeeping has become a popular alternative to in-house bookkeeping
- Top reasons our clients use our remote accounting services:
 - Managing finances distracts the organization from its mission
 - Leadership and member increased confidence in their finances
 - Tax and accounting regulations are complex and changing faster than ever
 - They want a trusted advisor to provide CPA oversight



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We're hiring!

- Audit, tax, and accounting assistance duties include:
 - Assist clients with accounting, QuickBooks, and tax preparation
 - Perform financial statement compilations, reviews, and audits
 - Review and reconcile general ledger accounts
 - Interact with clients and work collaboratively with team members
- View our job openings on [our website](#) or send your resume to info@battershellnichols.com



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- *The author is not engaged by this text or webinar in the rendering of tax, accounting, or similar professional services.*
- *While the tax, and accounting issues discussed in this material have been reviewed with sources believed to be reliable, concepts discussed can be affected by changes in the law or in the interpretation of such laws since this text was printed. For that reason, the accuracy and completeness of this information and the opinions based thereon cannot be guaranteed.*
- *Before taking any action, all references and citations should be checked and updated accordingly.*



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Overview of Minister Taxation

February 2, 2022
By: Rick Battershell, CPA



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4 Basic Tax Changes

1. Social Security & Medicare Taxes
2. Federal Income Taxes
3. Housing Allowance
4. Self-Employment Taxes



Basic Tax Decisions

1. **Federal Income Taxes** – how much to withhold
 - Use Form W-4 to notify payroll department
2. **Housing Allowance** – ask church to designate an amount
3. **Self-Employment Taxes** – whether to elect out

Sample Pay Check

	Lay Employee	Minister Employee
Wages	100.00	100.00
Social Sec Tax	-6.20	n/a
Medicare Tax	-1.45	n/a
Federal Income Tax	<u>-15.00</u>	<u>(minister's option)</u>
Net Payroll	77.35	100.00

Tax Mistakes Ministers Make

- Tax Status
 - Reporting income/expenses on Schedule C when they are employees
 - Reporting compensation on a W-2 with SS/Medicare tax withholding
 - Receiving a Form 1099 rather than a W-2
- Housing Allowance Errors:
 - No portion of compensation is allocated as housing
 - Mid-year change of status
 - Not treating it as subject to self-employment tax
 - Not considering the rental value limitation

Tax Mistakes Ministers Make

- Business Expenses
 - Not logging business miles driven (receive allowance)
 - Not documenting and submitting reimbursable business expenses
 - Business purpose, business relationship
- Filing for SE tax exemption when not qualified to opt out



Social Security & Medicare Benefits Funding

- Primarily funded through:
 - Payroll taxes (FICA):
 - ½ paid by Employee
 - ½ paid by Employer
 - Self-employment taxes (SECA)
 - Independent contractors (and ministers)
 - Pay both employee and employer share of the tax

Social Security Benefits Calculation



- Simple overview:
 - List your historical social security wages
 - Adjust historical wages to = current equivalent dollars

Social Security Benefits Calculation

- Simple overview continued
 - Compute average of your highest 35 years of indexed Social Security wages
 - Look up this 35 year average of highest wages in a SSA table
 - Equals Social Security benefit at normal retirement age 67 if born in 1960 or after)

SE Tax Exemption for Ministers

Form 4361 (Rev. January 2011) Department of the Treasury Internal Revenue Service	Application for Exemption From Self-Employment Tax for Use by Ministers, Members of Religious Orders and Christian Science Practitioners	OMB No. 1545-0074 File Original and Two Copies
File original and two copies and attach supporting documents. This exemption is granted only if the IRS returns a copy to you marked "approved."		
Please type or print	1 Name of taxpayer applying for exemption (as shown on Form 1040)	Social security number
	Number and street (including apt. no.)	Telephone number (optional)
	City or town, state, and ZIP code	
	2 Check one box: <input type="checkbox"/> Christian Science practitioner <input type="checkbox"/> Ordained minister, priest, rabbi <input type="checkbox"/> Member of religious order not under a vow of poverty <input type="checkbox"/> Commissioned or licensed minister (see line 6)	3 Date ordained, licensed, etc. (Attach supporting document. See instructions.)
	4 Legal name of ordaining, licensing, or commissioning body or religious order	
	Number, street, and room or suite no.	Employer identification number
	City or town, state, and ZIP code	
	5 Enter the first 2 years after the date shown on line 3 that you had net self-employment earnings of \$400 or more, any of which came from services as a minister, priest, rabbi, etc.; member of a religious order; or Christian Science practitioner	
	6 If you apply for the exemption as a licensed or commissioned minister and your denomination also ordains ministers, please indicate how your ecclesiastical powers differ from those of an ordained minister of your denomination. Attach a copy of your denomination's bylaws relating to the powers of ordained, commissioned, and licensed ministers.	
	7 I certify that I am conscientiously opposed to, or because of my religious principles I am opposed to, the acceptance (for services I perform as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner) of any public insurance that makes payments in the event of death, disability, old age, or retirement; or that makes payments toward the cost of, or provides services for, medical care. (Public insurance includes insurance systems established by the Social Security Act.) I certify that as a duly ordained, commissioned, or licensed minister of a church or a member of a religious order not under a vow of poverty, I have informed the ordaining, commissioning, or licensing body of my church or order that I am conscientiously opposed to, or because of religious principles I am opposed to, the acceptance (for services I perform as a minister or as a member of a religious order) of any public insurance that makes payments in the event of death, disability, old age, or retirement; or that makes payments toward the cost of, or provides services for, medical care, including the benefits of any insurance system established by the Social Security Act. I certify that I have never filed Form 2031 to revoke a previous exemption from social security coverage on earnings as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner. I request to be exempted from paying self-employment tax on my earnings from services as a minister, member of a religious order not under a vow of poverty, or Christian Science practitioner, under section 1402(e) of the Internal Revenue Code. I understand that the exemption, if granted, will apply only to these earnings. Under penalties of perjury, I declare that I have examined this application and to the best of my knowledge and belief, it is true and correct.	
	Signature ►	Date ►

SE Tax Exemption for Ministers

- IRS Form 4361 Application for Exemption Qualifications:
 1. Minister status – commissioned, licensed, or ordained by a church or association of churches
 2. Opposed to accepting social security benefits for services as a minister based on religious principles
 - Reason for election cannot be financial
 3. Did not make prior election to be covered under Social Security (e.g. form 2031)

SE Tax Exemption for Ministers

- Form 4361 Exemption Qualifications continued
 4. Notify the church body that you are filing Form 4361 and are opposed to Social Security for services as a minister.
 5. File Form 4361 by the federal income tax due date for the 2nd year the minister has net SE earnings of \$400 or more (including services as a minister)
 6. IRS verification letter signed and returned (send via certified mail)

Tax computation Example

	Lay Employee	Minister Pays SE Tax	Minister elected out of SE Tax
Salary as Employee	65,000	65,000	65,000
Housing allowance	0	-25,000	-25,000
Self Empl tax deduction	0	-4,592	0
Standard deduction MFJ	-25,100	-25,100	-25,100
Taxable Income	<u>39,900</u>	<u>10,308</u>	<u>14,900</u>
Income tax at 15%	7,395	1,033	1,493
Soc Sec & Medicare Taxes	4,393	0	0
Self Employment tax	<u>0</u>	<u>9,184</u>	<u>0</u>
Total tax	11,788	10,217	1,493

Reducing Self-Employment Tax

- Minister strategies:
 - Deduct clergy related business expenses
 - Salary reduction to 403(b)



Clergy Related Business Expenses

- No miscellaneous itemized 2018-2025
- SE tax calculation allows deductions for:
 - Mileage rates 56 cents per business mile in 2021
 - 2022 = 58.5 cents
 - Cell phones – business use
 - Other unreimbursed business related costs

Housing Allowance Basics

- Only available to ministers
- Church employer designates a portion of a minister's compensation as housing allowance
- Applies prospectively, not retroactively
 - Request designation for more than anticipated costs

Housing Allowance

- Housing Costs – Which Home?
 - IRS interprets this to mean your primary residence
 - Tax court case– does not apply to 2nd home



Housing Costs

- **Includes:**

- Mortgage payments or rent
- Insurance (home or renters)
- Property taxes
- Utilities
- Furnishings & appliances
- Repairs, yard maintenance, etc

- **Excludes:**

- Food & food preparation
- Child care
- Cell phone

Housing Allowance

- Housing Costs:
 - Planning major addition/remodel
 - Spread the costs over multiple years
 - Financing addition?
Housing cost is when loan paid



Housing Allowance



Housing costs do not include:

- If renting a portion of the home, costs do not include those allocated to the rented portion

Housing Allowance

- Exclude from taxable income (lesser of):
 - Housing costs
 - Designated housing allowance
 - Rental value



Sample Computation

Scenarios	1	2	3
Housing Costs	32,000	32,000	32,000
Church Designation	30,000	35,000	35,000
Rental Value (furnished with utilities)	31,000	31,000	32,500
Amount Excluded from Taxable Income	30,000	31,000	32,000
Taxable as "Excess Housing Allowance"	0	4,000	3,000

403(b) Retirement Plans



- Housing allowance designation in retirement
 - Church retirement plan can designate a portion or all of distributions as “housing”
 - Benefits do not apply to non-clergy spouse upon death of pastor

403(b) Retirement Plans

- Employee Elective Deferral Contributions:
 - General rule in 2021 = \$19,500, 2022 = \$20,500
 - Extra \$6,500 if over 50 years old
 - Can designate these as Roth contributions (but doesn't reduce SE Tax)
 - In some situations, an extra \$3,000 may be available if employed by church more than 15 years

Structuring Minister Compensation to Minimize Taxes

- Consider providing nontaxable benefits:
 - Cell phones
 - Computer and laptop
 - Reimburse mileage vs providing an auto allowance
 - Business expense reimbursements under an accountable plan
 - Health insurance, reimbursements, HSA
 - 403(b) retirement plan
 - Adoption assistance
 - Dependent care

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Next Webinar



March 16, 2022

TBD: Check our website or watch for future emails



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Thank you for joining us

Please reach out with any questions:

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